

Message Text

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ACTION EUR-12

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TO SECSTATE WASHDC 8790
TREASURY DEPT WASHDC
INFO AMEMBASSY BONN
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AMEMBASSY DUBLIN
AMEMBASSY PARIS
AMEMBASSY ROME
AMEMBASSY TOKYO
AMCONSUL BELFAST
AMCONSUL EDINBURGH
USMISSION GENEVA
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DEPARTMENT PASS FEDERAL RESERVE BOARD; TREASURY FOR
DONALD E. SYVRUD, OASIA

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SUBJECT: PRESS REACTION TO PROPOSED INCREASES IN THE PRT
REF: LONDON 12329

EDITORIAL REACTION TO THE GOVERNMENT'S PLANS TO RAISE THE
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PETROLEUM REVENUE TAX WAS CAUTIOUS WITH MIXED ASSESSMENT.
IT IS CONTENDED THAT ALTHOUGH THE COST TO THE OIL COM-
PANIES DOES NOT APPEAR SEVERE, THE CHANGES COULD AFFECT
SOME FIELDS MORE SHARPLY THAN OTHERS AND NOTICEABLY RE-
VISES THE GOVERNMENT SHARE OF NORTH SEA OIL REVENUE.

1. THE TIMES FINANCIAL EDITOR WRITES:

QUOTE: UNDEMANDING CHANGES. OIL COMPANIES AND THEIR SHARE HOLDERS CAN BREATHE A SIGH OF RELIEF. CHANGES IN PETROLEUM REVENUE TAX ANNOUNCED YESTERDAY -- IF THEY SURVIVE AN ELECTION -- WILL BE MILD BOTH IN THEIR EFFECTS ON PROFITS FROM EXISTING NORTH SEA DEVELOPMENTS AND ON FUTURE EXPLORATION. THE INCREASED GOVERNMENT TAKE, THOUGH NOT INSIGNIFICANT, IS NOT AS GREAT AS A 15 PERCENT RISE IN THE PRT RATE TO 60 PERCENT WOULD IMPLY.

TOTAL REVENUES FROM NORTH SEA TAX TO THE MID-L980S WILL BE LESS THAN TEN PERCENT GREATER THAN THEY ARE UNDER PRESENT RULES AND IN 1979-89, ALTHOUGH THE TAKE FROM PRT WILL NEARLY DOUBLE, THE 150 MILLION POUND INCREASE IS ONLY WHAT IT COSTS TO BUILD THE BOILERS FOR THE DRAX B POWER STATION.

UNDER THE NEW RATES AND SLIGHTLY CHANGED ALLOWANCES, THE TOTAL TAKE OF NORTH SEA COMPANY PROFITS IS ESTIMATED ULTIMATELY TO INCREASE FROM 70 TO 75 PERCENT: A REDUCTION OF A SIXTH IN AFTER TAX PROFITS WHICH WILL HARDLY BE WELCOMED, BUT WITH FIELDS LIKE FORTIES PROVING MORE PROFITABLE THAN EXPECTED, THIS IS NOT EXCESSIVE.

AND THE SAFEGUARDS ON THE ANNUAL LIMITS OF TAX PAYABLE AND THE RESTATEMENT YESTERDAY OF THE GOVERNMENT'S WILLINGNESS TO LIFT ROYALTIES ON MARGINAL FIELDS SHOULD LEAVE MANY SMALLER FIELDS AS THEY WERE -- NEVER LIKELY TO PAY ANY PRT.

FOR BP THE INCREASED RATE WILL IMPACT NEXT YEAR BUT UNCLASSIFIED

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IT ESCAPES THE EFFECTS OF THE REDUCTION IN CAPITAL ALLOWANCES FROM 175 PERCENT TO 135 PERCENT WHICH AFFECTS ONLY NEW FIELDS. PRT IS ALLOWABLE AGAINST CORPORATION TAX AND BP WILL BE GETTING INCREASED ALLOWANCES AGAINST CORPORATION TAX AS MAGNUS IS DEVELOPED, SO THERE WILL BE A COMPLICATED TRADE OFF, BUT ONE WHICH WILL UNDOUBTEDLY MAKE THE TAX INCREASE LESS THAN IT MIGHT APPEAR AT FIRST SIGHT. SHELL, ON THE OTHER HAND, IS UNLIKELY TO BE LIABLE TO PRT PAYMENTS FOR SOME TIME. END QUOTE.

2. THE FINANCIAL TIMES LEAD EDITORIAL READS:

QUOTE: CHANGING THE RULES. THERE IS NO REASON IN PRINCIPLE WHY THE GOVERNMENT SHOULD NOT REVIEW THE ARRANGEMENTS FOR TAXING THE PROFITS OF OIL COMPANIES OPERATING IN THE NORTH SEA. THE PETROLEUM REVENUE TAX WAS CONCEIVED AS A FORM OF EXCESS PROFITS LEVY. IT WAS INTRODUCED IN 1975, AND A "RING FENCE" WAS DRAWN AROUND AN OIL COMPANY'S NORTH SEA OPERATIONS FOR CORPORATION TAX PURPOSES, PARTLY BECAUSE IT WAS FELT THAT THE SCALES HAD PREVIOUSLY BEEN WEIGHTED TOO MUCH IN FAVOUR OF THE COMPANIES WHICH HAD BEEN GRANTED GOVERNMENT LICENSES TO EXTRACT OIL AND PARTLY BECAUSE OF THE FURTHER SUBSTANTIAL

PROFITS THEY WERE EXPECTED TO MAKE AS A RESULT OF THE
QUADRUPLING OF OIL PRICES IN 1973-74.

MARGINAL. AFTER THREE YEARS' EXPERIENCE, THE GOV-
ERNMENT BELIEVES THAT ITS APPROACH HAD STILL BEEN TOO
CAUTIOUS AND THAT A GREATER SHARE OF THE BENEFITS OUGHT

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TO ACCRUE IN THE FORM OF TAX REVENUE. THAT COULD WELL
BE,ALTHOUGH IT HAS NOT PRODUCED ANY EVIDENCE ON WHICH THE
PUBLIC CAN JUDGE. WHAT IS MORE REMARKABLE, HOWEVER, IS
THE NATURE OF THE CHANGES THE GOVERNMENT IS PROPOSING TO
MAKE TO THE PETROLEUM REVENUE TAX. THEY ARE LIKELY TO
BEAR MORE HEAVILY UPON THE SMALLER, MORE MARGINAL, FIELDS
WHICH HAVE YET TO BE DEVELOPED THAN UPON THE EARLIER AND
MORE PROFITABLE FIELDS, THE CURRENT POST-TAX EARNINGS
FROM WHICH PROMPTED THE PRESENT REVIEW. IF THERE WERE ANY

DOUBT ABOUT THIS, ONE HAS ONLY TO EXAMINE THE EXAMPLES
THAT WERE ISSUED YESTERDAY TO ILLUSTRATE THE EFFECTS OF
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THE PROPOSED CHANGES.

THE REASON FOR THIS IS PARTLY A DESIRE TO AVOID
INTRODUCING RETROACTIVE LEGISLATION, WHICH IS COMMEND-
ABLE ENOUGH. BUT IT ALSO STEMS FROM THE NATURE OF THE
TAX REGIME IMPOSED UPON NORTH SEA OPERATORS. THEY ARE
PAYING ROYALTIES AND CORPORATION TAX AS WELL AS THE PE-
TROLEUM REVENUE TAX. ROYALTY PAYMENTS ARE HOWEVER BASED
UPON THE QUANTITY OF OIL THEY PRODUCE RATHER THAN THE
PROFITS THEY EARN; AND IT WOULD BE DIFFICULT TO CHANGE
THE CORPORATION TAX PROVISIONS WHICH ARE HELPING SOME OP-
ERATORS TO REDUCE THEIR CURRENT (ALTHOUGH NOT THEIR
EVENTUAL) TAX BURDEN -- FOR EXAMPLE, THE RIGHT TO OFFSET
THE COST OF DEVELOPING NEW FIELDS AGAINST THE PROFITS
FROM EXISTING ONES -- WITHOUT RADICALLY ALTERING THE
STRUCTURE OF CORPORATION TAX AND THUS ITS APPLICATION TO
OTHER SECTORS OF INDUSTRY.

IF THE GOVERNMENT WANTS TO INCREASE ITS TOTAL TAX
TAKE FROM NORTH SEA OIL IT IS THEREFORE LARGELY LIMITED
TO MAKING CHANGES IN THE PETROLEUM REVENUE TAX. ... ALL
IN ALL, MINISTERS EXPECT THE CHANGES TO INCREASE THE TO-
TAL TAX TAKE BY ABOUT 10 PERCENT BY THE MID-1980S, RAIS-
ING THE AVERAGE TAX TAKE FROM EACH OPERATOR FROM ABOUT
70 PERCENT OF GROSS PROFITS TO ABOUT 75 PERCENT. BUT
THE INCREASE WILL BE GREATER FOR THE OPERATORS OF NEW
FIELDS.

UNCERTAINTY. WHETHER THE GOVERNMENT HAS IN FACT
PITCHED ITS DEMANDS TOO HIGH TO LEAVE SUFFICIENT INCEN-
TIVE FOR THE DEVELOPMENT OF SMALLER AND MORE MARGINAL
FIELDS IS HARD TO JUDGE AT THIS STAGE. THE 30 PERCENT
RETURN ON CAPITAL AND OTHER SAFEGUARD PROVISIONS DESIGNED
FOR MARGINAL FIELDS REMAIN, AND OPERATORS CAN CLAIM RE-
LIEF FROM ROYALTY PAYMENTS, AS THE CHIEF SECRETARY TO THE
TREASURY HAS SAID. BUT THE CHANGES IN PRT ARE ONLY THE
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LATEST OF A SERIES OF NEW TERMS AND CONDITIONS THE GOVERN-
MENT HAS INTRODUCED CONCERNING BNOC PARTICIPATION RIGHTS,
DEPLETION RATES, WASTE GAS FLARING, AND SO FORTH. THE
WORST THING FOR BUSINESS, PARTICULARLY IN AN AREA OF OP-
ERATION ALREADY AS UNPREDICTABLE AS THE NORTH SEA IS UN-
CERTAINTY. THE GOVERNMENT, OR ITS SUCCESSOR, WOULD BE
WISE TO BEAR THAT IN MIND BEFORE DECIDING THE FINAL SHAPE

OF ANY CHANGES IN NORTH SEA TAXATION. END QUOTE.

3. THE LEX COLUMN OF THE FINANCIAL TIMES MUSES:

QUOTE: ... OIL TAX. AT FIRST SIGHT THE GOVERNMENT'S PROPOSALS FOR INCREASING THE TAX TAKE FROM NORTH SEA OIL DO NOT LOOK PARTICULARLY TOUGH. BUT THE LOGIC BEHIND THE PLAN SEEMS TO BE TO SPLIT TOTAL PROFITS FROM THE NORTH SEA IN THE RATIO OF 75 TO THE GOVERNMENT AND 25 TO THE OIL COMPANIES. THIS COMPARES WITH THE OLD TARGET OF 70:30 AND AN OUTCOME WHICH LOOKED MORE LIKE 67:33 IF NO CHANGES WERE MADE. ON THE BASIS OF THESE ASSUMPTIONS THE OVER-ALL EFFECT OF YESTERDAY'S CHANGES IS A REDUCTION IN NORTH SEA EARNING OF AS MUCH AS 25 PERCENT. THE OTHER SIDE OF THE CALCULATION IS THAT THE GOVERNMENT TAX TAKE WILL INCREASE BY 10 PERCENT OVER THE NEXT SEVEN YEARS, TO RUN AT AN ANNUAL LEVEL OF 4.5 BILLION POUNDS FROM THE MID-80S.

... WHERE THE CHANGE, IF IT HAPPENS, WILL REALLY BE FELT IS ON THE DEVELOPMENT OF NEW FIELDS. UNDER THE PROPOSED TERMS IT WILL BE MUCH HARDER TO COVER INITIAL FINANCE COSTS ON FIELDS THAT ARE ANYWAY LIKELY TO BECOME INCREASINGLY DIFFICULT TO DEVELOP. END QUOTE.

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